



BOARD OF EQUALIZATION

BUSINESS TAXES COMMITTEE MEETING MINUTES

HONORABLE JOHN CHIANG, COMMITTEE CHAIR

450 N STREET, SACRAMENTO

MEETING DATE: MARCH 28, 2006, TIME: 9:30 A.M.

ACTION ITEMS & STATUS REPORT ITEMS

Agenda Item No: 1

Title: Proposed new regulations 1125 and 1423, *Two-party Exchange*, and proposed revisions to Regulations 1123 and 1420, *Supplier*, regarding the primary liability of payment of the fuel tax in a two-party exchange of fuel.

Issue/Topic:

Should the State Board of Equalization (Board) adopt Regulation 1125 and Regulation 1423 and amend Regulation 1123 and Regulation 1420 to make the receiving supplier primarily liable for payment of the fuel tax in a two-party exchange of fuel?

Committee Discussion:

Discussion of the agenda was as follows:

Action 1. Consent Items

There was no discussion on this item.

Action 2. Authorization to Publish

There was no discussion on this item.

Committee Action/Recommendation/Direction:

Action 1. Consent Items

The committee approved all consent items.

Action 2. Authorization to Publish

The committee recommended that the Board authorizes publication of the new proposed Regulation 1125, and Regulation 1423 and the proposed revisions to Regulation 1123 and Regulation 1420 as adopted by above action. The operative date of the new regulations and amendments is January 1, 2007. Implementation will take place 30 days after approval by the Office of Administrative Law.

Approved: /s/ John Chiang
Honorable John Chiang, Committee Chair

/s/ Ramon J. Hirsig
Ramon J. Hirsig, Executive Director

at the March 29, 2006 Board Meeting

/s/ Gary Evans

Deborah Pellegrini, Chief
Board Proceedings Division

MOTOR VEHICLE FUEL TAX LAW
Proposed amendment to Regulation 1123

Regulation 1123. SUPPLIER.

(a) RETURNS. All suppliers must prepare and file returns with the Board to report tax on motor vehicle fuel. Returns are due at the end of the month following the calendar month in which the motor vehicle fuel was removed, entered, or sold, unless the Board requires that a return be filed for a different period. A terminal operator who also is a position holder in motor vehicle fuel within the terminal or is jointly and severally liable for the tax is required to file both the terminal operator report and the supplier return.

(b) IMPOSITION OF TAX. Tax applies to each supplier as follows:

(1) **BLENDER.** A blender is required to pay the tax on the removal or sale of motor vehicle fuel blended outside the bulk transfer/terminal system. The number of gallons of blended motor vehicle fuel subject to the tax is the difference between the total number of gallons of blended motor vehicle fuel removed or sold and the number of gallons of tax-paid motor vehicle fuel used to produce the blended motor vehicle fuel.

(2) **ENTERER.**

(A) An enterer is required to pay the tax when the enterer imports motor vehicle fuel into the state by means outside of the bulk transfer/terminal system.

(B) An enterer is required to pay the tax when the enterer removes or sells motor vehicle fuel within a pipeline or terminal to an unlicensed person.

(C) An enterer is required to pay the tax when the entry is by bulk transfer and the enterer is not a licensed supplier.

(D) For purposes of proper imposition of tax, entry occurs when fuel is brought into the state, provided, however, that when entry is by bulk transfer, entry occurs as follows:

1. When fuel is received at a marine terminal, entry occurs at the landside of the flange.

2. When fuel is removed from a vessel in this state to a lighter for the purpose of lightering, entry occurs at the vessel side of the flange upon the removal of fuel from a vessel in this state to the lighter; provided, however, that if the lighter unloads or discharges the fuel at a marine terminal, then entry occurs at the land side of the flange as to the fuel received at the marine terminal. As used herein, "lightering" is the use of small, shallow-draft boats in transshipment to shore of oil or other fuel from a large,

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deep-draft vessel unable to dock at shore facilities because of shallow water. The small boats are called lighters.

3. When fuel is removed from a vessel in this state to another vessel in this state, and the fuel is not unloaded or discharged at a marine terminal, then entry occurs when the fuel is brought into the state.

(3) POSITION HOLDER.

(A) A position holder that holds an inventory position in the motor vehicle fuel as reflected on the records of the terminal operator is required to pay the tax when the motor vehicle fuel is removed from the terminal rack.

(B) A position holder is required to pay the tax when the position holder removes or sells motor vehicle fuel within or without the bulk transfer/terminal system to an unlicensed person.

(C) For reporting periods commencing on or after January 1, 2007, a position holder that delivers motor vehicle fuel to a receiving supplier under a two-party exchange contract shall remain liable for the tax due on the removal of motor vehicle fuel from the terminal rack unless all Regulation 1125 requirements are met.

(4) REFINER.

(A) A refiner is required to pay the tax when the motor vehicle fuel is removed at a terminal rack located at a refinery.

(B) A refiner is also required to pay the tax when the removal of motor vehicle fuel is by bulk transfer (e.g., transfer by pipeline or vessel) and the refiner or the owner of the motor vehicle fuel immediately before the removal is not a licensed supplier.

(C) A refiner is required to pay the tax when the refiner removes or sells motor vehicle fuel within or without the bulk transfer/terminal system to an unlicensed person.

(D) For reporting periods commencing on or after January 1, 2007, a refiner that delivers motor vehicle fuel to a receiving supplier under a two-party exchange contract shall remain liable for the tax due on the removal of motor vehicle fuel from the terminal rack located at a refinery unless all Regulation 1125 requirements are met.

(5) TERMINAL OPERATOR. A terminal operator is jointly and severally liable for and may be required to pay the tax when the motor vehicle fuel is removed at the rack if both subsections (A) and (B) below apply:

(A) The position holder with respect to the motor vehicle fuel is a person other than the terminal operator and is not a licensed supplier.

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(B) The terminal operator is not a licensed supplier and either (i) does not have an unexpired notification certificate from the position holder as required by the Internal Revenue Service or (ii) has an unexpired notification certificate from the position holder, but has reason to believe or knows that any information in the certificate is false.

(6) THROUGHPUTTER. A throughputter is required to pay the tax when the throughputter removes or sells motor vehicle fuel within or without the bulk transfer/terminal system to a person who is not a licensed supplier.

Authority: Sections 7372 and 8251 Revenue and Taxation Code

Reference: Sections 7307, 7308, 7309, 7310, 7311, 7312, 7324, 7326, 7329, 7332, 7333, 7334, 7335, 7336, 7338, 7339, 7340, 7341, 7360, 7362, 7363, 7365, 7366, 7368, 7369, 7370, 7371, 7372, 7451, 7651, and 7652.5, Revenue and Taxation Code.

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MOTOR VEHICLE FUEL TAX LAW

Proposed Regulation 1125

Regulation 1125. TWO-PARTY EXCHANGE**(a) GENERAL.**

In a typical two-party exchange, two suppliers who own motor vehicle fuel in terminals, i.e., who are position holders (pursuant to Section 7332 of the Revenue and Taxation Code), agree to give each other access to the motor vehicle fuel each owns. Both suppliers have customers in the same terminal areas. One supplier (the delivering supplier) owns fuel in one terminal, and the other supplier (the receiving supplier) owns fuel, usually in a different terminal. Each supplier agrees to exchange fuel it owns for fuel the other supplier owns. A two-party exchange contract allows each supplier to have rack removal capability at a terminal where the other supplier is a position holder, in order to supply fuel to its customers in that terminal area. The receiving supplier takes the place of the delivering supplier when the motor vehicle fuel is removed from the terminal at the rack. A two-party exchange may involve fuel held in terminals located in one or more states and may involve one or more types of fuel. For purposes of this regulation, however, at least one of the terminals involved in a two-party exchange must be located in this state, and the requirements for reporting transactions to the Board pursuant to this regulation pertain only to transactions involving terminals located in this state.

(b) DEFINITIONS.

(1) Notwithstanding Section 7337 of the Revenue and Taxation Code, “two-party exchange” means a transaction, other than a sale, that occurs at the time of removal of motor vehicle fuel across the rack and that meets all the following conditions:

(A) The terminal operator, delivering supplier, and the receiving supplier are each registered with the Board to file electronically and have filed electronically with respect to the subject two-party exchange; and

(B) The terminal operator treats the receiving supplier in its books and records as the person that removes the motor vehicle fuel across a terminal rack for purposes of reporting the two-party exchange to the Board; and

(C) The two-party exchange is the subject of a written contract between the delivering supplier and the receiving supplier, acceptable evidence of which includes, but is not limited to, exchange statements, exchange differential invoices, exchange reconciliations, or any other similar writing between the parties; and

(D) All of the reporting requirements set forth in subdivisions (d) and (e) of this section are met.

The proposed regulations and amendments contained in this document may not be adopted. Any revisions that are adopted may differ from this text.

(2) “Delivering supplier” means a supplier, licensed pursuant to Section 7451 of the Revenue and Taxation Code, who is the position holder of the motor vehicle fuel in the terminal on whom the motor vehicle fuel tax is imposed on removal of motor vehicle fuel from the rack for all purposes other than for a two-party exchange.

(3) “Receiving supplier” means a supplier, licensed pursuant to Section 7451 of the Revenue and Taxation Code, on whom the motor vehicle fuel tax is imposed only on removal of motor vehicle fuel from the rack as the receiving supplier under a two-party exchange.

(4) “Terminal,” as defined in Section 7339 of the Revenue and Taxation Code, includes, for purposes of this regulation, a terminal located at a refinery.

(c) LIABILITY FOR TAX.

(1) The delivering supplier is primarily liable for taxes imposed under Section 7362 or Section 7363(a) of the Revenue and Taxation Code, except, when a transaction satisfies the conditions and requirements for a two-party exchange, the delivering supplier shall be relieved of motor vehicle fuel tax liability and the receiving supplier shall become primarily liable for payment of motor vehicle fuel taxes on the motor vehicle fuel removed pursuant to the two-party exchange.

(2) The receiving supplier must report the two-party exchange and remit any tax due on a tax return filed within three months after the close of the calendar month in which the motor vehicle fuel was received. The receiving supplier may claim a refund for any amounts applied by the Board to the account of the receiving supplier under a two-party exchange contract. When all parties report a transaction as a two-party exchange, the receiving supplier may not file a claim for refund of the tax on the grounds that the transaction was not a two-party exchange.

(3) If the receiving supplier fails to report or remit taxes in conformity with this regulation, then the delivering supplier shall remain primarily liable for taxes due on the removal of the motor vehicle fuel from the rack.

(d) REPORTING REQUIREMENTS – GENERALLY.

(1) The terminal operator must report to the Board the two-party exchange of motor vehicle fuel between the delivering supplier and the receiving supplier.

(2) The terminal operator, the delivering supplier, and the receiving supplier must each use the same identifying information (e.g., bill of lading number) to refer to or otherwise report the subject two-party exchange.

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(3) The terminal operator, the delivering supplier, and the receiving supplier must each enter the same fuel type on any report that includes a two-party exchange.

(e) REPORTING REQUIREMENTS – DELIVERING AND RECEIVING SUPPLIERS. The following reporting requirements must be met in order for an exchange of motor vehicle fuel to qualify as a two-party exchange and to shift imposition of the motor vehicle fuel tax liability from the delivering supplier to the receiving supplier.

(1) The delivering supplier must report the two-party exchange and identify the receiving supplier to the terminal operator; and

(2) The delivering supplier must report to the Board a tax-free delivery of motor vehicle fuel to the receiving supplier; and

(3) The receiving supplier must report to the Board a tax-free receipt of motor vehicle fuel from the delivering supplier; and

(4) The receiving supplier must report to the Board the rack removal of motor vehicle fuel to its customers and the amount of tax due.

(f) OPERATIVE DATE. The provisions of this regulation are operative January 1, 2007.

Authority: Sections 7372 and 8251 Revenue and Taxation Code

Reference: Sections 7362, 7363, 7368, 7369, 7372, 7451, 7651, 7652.5, 8301, and 8302 Revenue and Taxation Code.

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DIESEL FUEL TAX LAW**Proposed Amendment to Regulation 1420****Regulation 1420. SUPPLIER.**

(a) RETURNS. All suppliers must prepare and file returns with the Board to report tax on diesel fuel. Returns are due at the end of the month following the calendar month in which the diesel fuel was removed, entered, or sold, unless the Board requires that a return be filed for a different period. A terminal operator who also is a position holder in diesel fuel within the terminal or is jointly and severally liable for the tax is required to file both the terminal operator return and the supplier return.

(b) IMPOSITION OF TAX. Tax applies to each supplier as follows:

(1) **BLENDER.** A blender is required to pay the tax on the removal or sale of diesel fuel blended outside the bulk transfer/terminal system. The number of gallons of blended diesel fuel subject to the tax is the difference between the total number of gallons of blended diesel fuel removed or sold and the number of gallons of tax-paid diesel fuel used to produce the blended fuel.

(2) **ENTERER.**

(A) An enterer is required to pay the tax when the enterer imports diesel fuel into the state by means outside of the bulk transfer/terminal system.

(B) An enterer is required to pay the tax when the enterer removes or sells diesel fuel within a pipeline or terminal to an unlicensed person.

(C) An enterer is required to pay the tax when the entry is by bulk transfer and the enterer is not a licensed supplier.

(D) For purposes of proper imposition of tax, entry occurs when fuel is brought into the state, provided, however, that when entry is by bulk transfer, entry occurs as follows:

(1) When fuel is received at a marine terminal, entry occurs at the landside of the flange.

(2) When fuel is removed from a vessel in this state to a lighter for the purpose of lightering, entry occurs at the vessel side of the flange upon the removal of fuel from a vessel in this state to the lighter; provided, however, that if the lighter unloads or discharges the fuel at a marine terminal, then entry occurs at the land side of the flange as to the fuel received at the marine terminal. As used herein, "lightering" is the use of small, shallow-draft boats in transshipment to shore of oil or other fuel from a large,

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deep-draft vessel unable to dock at shore facilities because of shallow water. The small boats are called lighters.

(3) When fuel is removed from a vessel in this state to another vessel in this state, and the fuel is not unloaded or discharged at a marine terminal, then entry occurs when the fuel is brought into the state.

(3) POSITION HOLDER.

(A) A position holder that holds an inventory position in the diesel fuel as reflected on the records of the terminal operator is required to pay the tax when the diesel fuel is removed from the terminal rack.

(B) A position holder is required to pay the tax when the position holder removes or sells diesel fuel within or without the bulk transfer/terminal system to an unlicensed person.

(C) For reporting periods commencing on or after January 1, 2007, a position holder that delivers diesel fuel to a receiving supplier under a two-party exchange contract shall remain liable for the tax due on the removal of diesel fuel from the terminal rack unless all Regulation 1423 requirements are met.

(4) REFINER.

(A) A refiner is required to pay the tax when the diesel fuel is removed at a terminal rack located at a refinery.

(B) A refiner is required to pay the tax when the removal of diesel fuel is by bulk transfer (e.g., transfer by pipeline or vessel) and the refiner or the owner of the diesel fuel immediately before the removal is not a licensed supplier.

(C) A refiner is required to pay the tax when the refiner removes or sells diesel fuel within or without the bulk transfer/terminal system to an unlicensed person.

(D) For reporting periods commencing on or after January 1, 2007, a refiner that delivers diesel fuel to a receiving supplier under a two-party exchange contract shall remain liable for the tax due on the removal of diesel fuel from the terminal rack located at a refinery unless all Regulation 1423 requirements are met.

(5) TERMINAL OPERATOR. A terminal operator is jointly and severally liable for and may be required to pay the tax when the diesel fuel is removed at the rack if both subsections (A) and (B) below apply, or if subsection (C) applies:

(A) The position holder with respect to the diesel fuel is a person other than the terminal operator and is not a licensed supplier.

The proposed regulations and amendments contained in this document may not be adopted. Any revisions that are adopted may differ from this text.

(B) The terminal operator is not a licensed supplier and either (i) does not have an unexpired notification certificate from the position holder as required by the Internal Revenue Service or (ii) has an unexpired notification certificate from the position holder, but has reason to believe or knows that any information in the certificate is false.

(C) The terminal operator provides any person with a bill of lading, shipping paper, or similar document which falsely indicates that the undyed or unmarked diesel fuel which is removed from the terminal is dyed or marked in accordance with the United States Environmental Protection Agency or the Internal Revenue Service requirements.

(6) THROUGHPUTTER. A throughputter is required to pay the tax when the throughputter removes or sells diesel fuel within or without the bulk transfer/terminal system to a person who is not a licensed supplier.

Authority: Sections 60063 and 60601 Revenue and Taxation Code

Reference: Sections 60003, 60004, 60006, 60007, 60008, 60009, 60010, 60011, 60012, 60013, 60015, 60021, 60022, 60023, 60029, 60030, 60031, 60032, 60033, 60035, 60050, 60051, 60052, 60053, 60054, 60055, 60059, 60060, 60061, 60062, 60063, 60131, and 60201, Revenue and Taxation Code.

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DIESEL FUEL TAX LAW

Proposed Regulation 1423

Regulation 1423. TWO-PARTY EXCHANGE**(a) GENERAL.**

In a typical two-party exchange, two suppliers who own diesel fuel in terminals, i.e., who are position holders (pursuant to Section 60010 of the Revenue and Taxation Code), agree to give each other access to the diesel fuel each owns. Both suppliers have customers in the same terminal areas. One supplier (the delivering supplier) owns fuel in one terminal, and the other supplier (the receiving supplier) owns fuel, usually in a different terminal. Each supplier agrees to exchange fuel it owns for fuel the other supplier owns. A two-party exchange contract allows each supplier to have rack removal capability at a terminal where the other supplier is a position holder, in order to supply fuel to its customers in that terminal area. The receiving supplier takes the place of the delivering supplier when the diesel fuel is removed from the terminal at the rack. A two-party exchange may involve fuel held in terminals located in one or more states and may involve one or more types of fuel. For purposes of this regulation, however, at least one of the terminals involved in a two-party exchange must be located in this state, and the requirements for reporting transactions to the Board pursuant to this regulation pertain only to transactions involving terminals located in this state.

(b) DEFINITIONS.

(1) Notwithstanding Section 60048 of the Revenue and Taxation Code, “two-party exchange” means a transaction, other than a sale, that occurs at the time of removal of diesel fuel across the rack and that meets all the following conditions:

(A) The terminal operator, delivering supplier, and the receiving supplier are each registered with the Board to file electronically and have filed electronically with respect to the subject two-party exchange; and

(B) The terminal operator treats the receiving supplier in its books and records as the person that removes the diesel fuel across a terminal rack for purposes of reporting the two-party exchange to the Board; and

(C) The two-party exchange is the subject of a written contract between the delivering supplier and the receiving supplier, acceptable evidence of which includes, but is not limited to, exchange statements, exchange differential invoices, exchange reconciliations, or any other similar writing between the parties; and

(D) All of the reporting requirements set forth in subdivisions (d) and (e) of this section are met.

The proposed regulations and amendments contained in this document may not be adopted. Any revisions that are adopted may differ from this text.

(2) “Delivering supplier” means a supplier licensed pursuant to Section 60131 of the Revenue and Taxation Code, who is the position holder of the diesel fuel in the terminal on whom the diesel fuel tax is imposed on removal of diesel fuel from the rack for all purposes other than for a two-party exchange.

(3) “Receiving supplier” means a supplier licensed pursuant to Section 60131 of the Revenue and Taxation Code, on whom the diesel fuel tax is imposed only on removal of diesel fuel from the rack as the receiving supplier under a two-party exchange.

(4) “Terminal” as defined in Section 60033 of the Revenue and Taxation Code, includes, for purposes of this regulation, a terminal located at a refinery.

(c) LIABILITY FOR TAX.

(1) The delivering supplier is primarily liable for taxes imposed under Section 60051 or Section 60052(a) of the Revenue and Taxation Code, except, when a transaction satisfies the conditions and requirements for a two-party exchange, the delivering supplier shall be relieved of diesel fuel tax liability and the receiving supplier shall be liable for payment of diesel fuel taxes on the diesel fuel removed pursuant to the two-party exchange.

(2) The receiving supplier must report the two-party exchange and remit any tax due on a tax return filed within three months after the close of the calendar month in which the diesel fuel was received. The receiving supplier may claim a refund for any amounts applied by the Board to the account of the receiving supplier under a two-party exchange contract. When all parties report a transaction as a two-party exchange, the receiving supplier may not file a claim for refund of the tax on the grounds that the transaction was not a two-party exchange.

(3) If the receiving supplier fails to report or remit taxes in conformity with this regulation, then the delivering supplier shall remain primarily liable for taxes due on the removal of the diesel fuel from the rack.

(d) REPORTING REQUIREMENTS – GENERALLY.

(1) The terminal operator must report to the Board the two-party exchange of diesel fuel between the delivering supplier and the receiving supplier.

(2) The terminal operator, the delivering supplier, and the receiving supplier must each use the same identifying information (e.g., bill of lading number) to refer to or otherwise report the subject two-party exchange.

(3) The terminal operator, the delivering supplier, and the receiving supplier must each enter the same fuel type on any report that includes a two-party exchange.

The proposed regulations and amendments contained in this document may not be adopted. Any revisions that are adopted may differ from this text.

(e) REPORTING REQUIREMENTS – DELIVERING AND RECEIVING

SUPPLIERS. The following reporting requirements must be met in order for an exchange of diesel fuel to qualify as a two-party exchange and to shift the diesel fuel tax liability from the delivering supplier to the receiving supplier.

(1) The delivering supplier must report the two-party exchange and identify the receiving supplier to the terminal operator; and

(2) The delivering supplier must report to the Board a tax-free delivery of diesel fuel to the receiving supplier; and

(3) The receiving supplier must report to the Board a tax-free receipt of diesel fuel from the delivering supplier; and

(4) The receiving supplier must report to the Board the rack removal of diesel fuel to its customers and the amount of tax due.

(f) OPERATIVE DATE. The provision of this regulation are operative January 1, 2007.

Authority: Sections 60063 and 60601 Revenue and Taxation Code

Reference: Section 60051, 60052, 60053, 60054, 60063, 60131, 60201, 60204, 60604, and 60605 Revenue and Taxation Code.

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